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Constitutionality of the
proposal in Senate bill 2906

CONSTITUTIONALITY OF THE PROPOSAL IN SENATE BILL 2906 (66th Cong., 1st Sess.) TO TAKE FROM A CARRIER A PART OF ITS EARNINGS ON LAWFUL RATES.

Opinion of
Charles Evans Hughes.

September 19, 1919.

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New York, September 19, 1919.

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DEAR SIR:

In reply to your request for my opinion as to the constitutionality of the provision in Section 6 of Senate Bill 2906 (66th Cong., 1st Sess.) entitled "A Bill further to regulate commerce among the States," etc., relating to the disposition of the described "excess" earnings of carriers, I beg to say:

Section 6 is as follows:

> "In dividing the country into districts and the carriers into rate-making groups the Commission shall have in view the similarity of transportation and traffic conditions therein. Rates of transportation shall at all times be just and reasonable. In changing or modify-

ing them from time to time in the manner provided in the Act to regulate commerce, as amended, and in viewing them from the standpoint of their effect in producing revenue in any rate-making group as a whole, the Commission shall take into consideration the interest of the public, the shippers, the wages of labor, the cost of maintenance and operation (including taxes), a fair return upon the value of the property in the group and used for or held for the service of transportation, the requirements for additional capital in order to enable the carriers to adequately perform their duties to the public and the conditions under which the same can be secured; and, for the purposes aforesaid, the Commission shall from time to time determine the value of the property in each district and so lower or advance the rates of transportation, as nearly as may be, to provide said fair return as herein provided.

"If any carrier shall receive from operation in any year more than a fair return, to be determined by the Commission, upon the value of its property, held or used for service in transportation, which may include a just allowance to provide reasonably for future years in which there may be insufficient earnings; the excess above such fair return shall be paid to the Board within the first four months of the succeeding year, to be invested or expended for the following purposes, namely: One-half of all such payments to the Board shall be invested or expended for the purposes set forth in Section 25 hereof, and one-half thereof shall be deposited in a fund which,

from time to time, shall be expended by the Board in the purchase of equipment to be leased under proper terms to carriers in order to facilitate transportation, or, to loan to carriers upon reasonable security in order to purchase equipment or other facilities in the event that such carriers are unable to secure elsewhere the funds with which to provide themselves with adequate transportation facilities. In no event shall surplus earnings in excess of the amount sufficient to pay a fair dividend, whether represented in reserves or otherwise invested in the property of the carrier, be capitalized or used in any way as a basis for increased rates.

"In applying the foregoing rule a comprehensive view of the rate-making group shall be taken and the level of rates, fares, and charges shall be determined with reasonable reference to average conditions therein."

I assume that it is the intent of the provision as to the payment by a carrier of "excess" earnings to the Railway Transportation Board that the one-half, which is to be put by that Board into the Employees' Welfare Fund, is to be used under Section 25 of the Bill for the benefit of railway employees generally and not separately for the benefit of the employees of the particular carrier paying the "excess"; and that the other one-half of the "excess" earnings which is to be used otherwise by the Board may be used in the purchase of equipment to be leased, or in the making of loans, to carriers other than the carrier making the payment. In short, it is the essence of the provision

that the so-called "excess" earnings of a carrier may be required to be paid to a government agency for the purpose of being used by that agency not only for the general benefit of railway employees but for the benefit of other carriers.

It should be observed that this requirement is not made as a condition for the exercise of any franchise granted to the carrier by the Federal Government. It is to be considered in its application to carriers chartered by the States and entitled to engage in interstate commerce on compliance with such regulations as Congress may constitutionally prescribe. Under the doctrine of the recent decision in *Hammer v. Dagenhart* (247 U. S. 251), the right to engage in the business of transporting passengers, or of ordinary and wholesome commodities, between the States, while subject to appropriate regulation, may not be deemed to be subject to the absolute prohibition of Congress and hence is not to be regarded as a privilege to be granted on any terms Congress may see fit to impose.

Nor is the requirement with respect to "excess" earnings imposed as a condition of the enjoyment of any guaranty as to earnings which has been given by the Federal government and accepted by the carrier, thus constituting a contract governing the carrier's operations. The carrier still must take its risk of losses. If it be said in a general sense that the provisions as to rates constitute a guaranty of proper and adequate rates, this is no more than the promise of the reasonable exercise of the power of regulation.

There is no benefit conferred upon the carriers under the Bill which can be regarded as justifying an exaction which otherwise could not be enforced.

Further, the requirement as to the payment of "excess" earnings does not purport to be imposed under the taxing power and in my judgment could not, in its present form, be sustained as a valid tax independently of the power of regulation. It would seem to be clear that the constitutional authority which would be invoked in the enactment of this legislation would be solely the power of Congress to regulate interstate commerce.

The general principles governing the constitutional authority of Congress to regulate interstate commerce are not open to dispute. It is a power to foster, to protect, to conserve; to prescribe the rules by which interstate commerce shall be governed. It unquestionably embraces a broad authority to deal with all phases of transportation in interstate commerce and to govern the instrumentalities of that commerce, including the relation of carriers and their employees, as illustrated by the Hours of Service Act, the Employers' Liability Act and the Adamson Act as to hours and wages (*Baltimore & Ohio R. R. Co. v. Interstate Commerce,* 221 U. S. 612; *Second Employers' Liability Cases,* 223 U. S. 1; *Wilson v. New,* 243 U. S. 332). It is also well settled that the exercise of the power may be in the nature of police regulations (*Lottery Case,* 188 U. S. 321; *Hipolite Egg Co. v. United States,* 220 U. S. 45; *Caminetti v. United States,* 242 U. S. 470). But, in the most ex-

treme applications and under the broadest definitions of this Federal power it has been recognized that it is not an unqualified or arbitrary power. It must be exercised subject to the limitations of the Fifth Amendment of the Federal Constitution prohibiting the deprivation of any person of liberty or property without due process of law (*Monongahela Navigation Co. v. United States,* 148 U. S. 312, 336; *Clark Distilling Co. v. Western Maryland Railway Co.,* 242 U. S. 331, 332; *United States v. Cress,* 243 U. S. 316, 326).

The broad legislative discretion of Congress with respect to rates of transportation is thus subject to the limitation that the rates shall not be made so low as to be confiscatory (*Wilson v. New,* 243 U. S. 332, 349, and cases there cited). And aside from the imposition of confiscatory rates, the power to regulate does not justify the assertion of arbitrary control, however excellent the motive, that is, an exercise of power not appropriate to the subject (*Adair v. United States,* 208 U. S. 161, 178, 180; *Interstate Commerce Commission v. Chicago G. W. Railway Company,* 209 U. S. 108, 118; *Southern Pacific Company v. Interstate Commerce Commission,* 219 U. S. 433, 444; *Interstate Commerce Commission v. Louisville & Nashville R. R. Co.,* 227 U. S. 88, 91; *Hammer v. Dagenhart,* 243 U. S. 251, 270, 276; *Wilson v. New,* 243 U. S. 332, 346). As was said in *Wilson v. New,* (243 U. S. 332, 346, 353) "It is equally certain that where a particular subject is within such authority, the extent of regulation depends on the nature and

character of the subject and what is appropriate to its regulation."

Having these general considerations in mind, the validity of the provision of the pending Bill as to the disposition of so-called "excess" earnings may be considered in the following aspects:

First: On the assumption that the rates as fixed by the Commission, under which the "excess" earnings have been realized, are just and reasonable rates.

It is to be borne in mind that rates fixed by competent legislative authority, which are not found to be confiscatory are presumed to be just and reasonable and that the courts do not interfere with the exercise of the legislative discretion, whether it be exercised directly by Congress or through its subordinate agency in accordance with the standards which Congress fixes (*Minnesota Rate Cases,* 230 U. S. 352, 433; *Wilson v. New,* 243 U. S. 332, 349).

Section 6 of the Bill provides that: "Rates of transportation shall at all times be just and reasonable." It is provided in Section 1 of the Bill that rates, fares and charges in force at the time of the repeal of the Federal Control Act of March 21, 1918, shall remain in force until changed by competent authority. It is further provided in Section 5 of the Bill that schedules of rates, fares and charges filed with the Commission in accordance with the "Act to regulate commerce" within thirty days after Federal control ceases shall become effective at the end of four months after they are so filed, with such modifications as may be ordered by the Commission, and the Commission is

required within that time to determine whether they shall be modified "in order to make them fair, just and reasonable rates for the service to be performed." It is further provided in Section 44 of the pending Bill, amending Section 15 of the "Act to regulate commerce," that whenever the Commission after a hearing either on complaint or on its own initiative shall be of opinion that any individual or joint rate, fare or charge whatsoever charged or collected by any carrier is or will be unjust or unreasonable the Commission is authorized to determine what will be the just and reasonable individual or joint rate, fare or charge to be thereafter observed, and the carrier is prohibited from making any charge which is in conflict with this determination. Thus all the rates fixed and maintained are at all times open to inquiry and the Commission has full authority to insist that the rates shall never be more than just and reasonable compensation for the services which the carrier renders. Nor does the Bill interfere with the reparation proceedings which may be entertained on the application of persons aggrieved by extortionate charges.

Taking all the provisions of the Bill into consideration, it would seem that the rates as fixed and permitted to be charged and collected by the carrier, assuming that the rates are not confiscatory, should be regarded as just and reasonable rates fixed and maintained by competent authority. It is also to be observed that Section 6 of the Bill providing for the payment to the Railway Transportation Board of the so-called "excess" earnings does not provide for a

determination that the rates under which the described "excess" has been collected by the carrier were not just and reasonable rates for the services rendered.

If, however, the rates thus fixed, charged and received by a carrier are to be deemed just and reasonable for the services rendered, the carrier is entitled to these receipts as its property, and the taking by the Government of any portion of these receipts (except under a valid tax) for general governmental purposes or for the benefit of other carriers would appear to be a taking of property contrary to the Fifth Amendment of the Federal Constitution.

Of course, a carrier may be required to render the service involved in its undertaking as a carrier. It may be required to spend whatever money is necessary to make such service prompt and adequate. Its conduct, in the performance of that service, may be regulated with respect to facilities for transportation, the hours of service of employees, standards of wages, liabilities for injuries, the health and comfort and safety of all persons concerned in the transportation, and the receipt, handling and delivering of commodities transported, but the requirement of the use of money for the manifold purposes which may be embraced in proper regulation, and the protection and conservation of interstate commerce, with respect to the carrier, are in connection with the performance of the carrier's service. In the present case it must be assumed that the carrier has met all its responsibilities under the law, has given all the required facili-

ties, has observed all regulations as to transportation, employees, passengers and goods, and has charged the just and reasonable rates established by law, and that the earnings that it has left are the proceeds of its reasonable contracts made in conformity with law.

I do not think that the provision of Section 6 as to "excess" earnings can be sustained under the principle of the case of *Charlotte, Columbia & Augusta R. Co. v. Gibbes,* 142 U. S. 386, and other similar cases, as to the placing of the expenses of governmental supervision upon the corporations supervised, or under the doctrine of the case of *Noble State Bank v. Haskell,* 219 U. S. 104, relating to an assessment under State law upon State banks for a depositors' guaranty fund, or of the case of *Mountain Timber Company v. Washington,* 243 U. S. 219, with respect to required contribution for a workman's compensation fund in order to provide compensation for injuries resulting from the hazards of the business. The provision in the pending Bill does not relate to the expenses of supervision. It is not an imposition in the nature of an occupation tax or a license tax. The assessment in the *Noble State Bank* case has been described by the Supreme Court of the United States as being in the nature of an occupation tax upon all banks existing under the laws of the State. (See 243 U.S.p.245.) In the *Mountain Timber* case the contributions for the workmen's compensation fund were required under the general police power of the State and these contributions were levied upon all employers in the described hazardous occupations according to per-

centages fixed in proportion to the hazards of each group. The provision of the pending Bill is not a tax laid upon all carriers with respect either to gross receipts, or net receipts, or any other basis for the assessment of a tax, but is simply a requirement of the payment to the Government Board of the "excess" earnings of a carrier which the Interstate Commerce Commission determines to be more than a "fair return" upon the value of its property. Such an exaction goes beyond the limits of any decision known to me, and if the rates under which the so-called "excess" earnings are collected by the carrier are to be deemed to be just and reasonable rates, fixed and maintained as such under the authority of law, I am unable to escape the conclusion that the requirement as to the payment of the so-called "excess" earnings of a carrier exceeds the constitutional authority of Congress as applied to carriers not transacting their business under a Federal franchise or contract imposing such a condition.

Second: It will doubtless be insisted, however, that the provision in question should be viewed in another aspect. It may be said that the rates under which the so-called "excess" earnings have been obtained are not to be deemed just and reasonable rates, and while they were charged and collected as such under authority of law, that the fixing of the rates as just and reasonable is only tentative.

The argument will undoubtedly be that the Bill requires the division of the country into districts and the carriers into "rate-making groups," and that Sec-

tion 6 requires the Commission to take a comprehensive view of the rate-making group and that the level of rates is to be determined with reasonable reference to average conditions. In viewing rates from the standpoint of their effect in producing revenue in any rate-making group as a whole, the Commission is directed to take into consideration the interest of the public, the shippers, the wages of labor, the cost of maintenance and operation (including taxes), a fair return upon the value of the property in the group and the requirements for additional capital in order to enable the carriers adequately to perform their duties to the public. Hence, it will be said that the rates fixed or maintained as just and reasonable for the services in question are fixed with reference to a group of carriers, and that so far as any particular carrier is concerned the finding as to the reasonableness of the rates charged by that carrier must be deemed to be merely a tentative finding. It will thus be contended that what is meant by the provision as to the payment to the Government Board of "excess" earnings is that no carrier shall be allowed to receive for its services more than what is subsequently determined by the Commission to be a "fair return" upon the value of its property held or used for the service; that all rates allowed are subject in the case of each carrier to this ultimate determination, and that to the extent that the rates produce the "excess" earnings they are to be deemed to be unreasonable. In this view it will be urged that no carrier is to be regarded as deprived of earnings from reasonable rates, but

only of the "excess" earnings under the rule of limitation; and that, further, as the amount which the particular carrier is permitted to retain is determined to be a fair return upon the value of its property, it cannot be said that there is an abuse of the regulatory power of Congress.

This argument encounters serious objections:

(1) It apparently takes no account of the fact that the individual rates charged by the carrier or the joint rates charged by the carrier in connection with other carriers may have been separately determined, either upon complaint or upon the Commission's initiative, to be just and reasonable rates for the services which the particular carrier renders. The provision as to the payment of "excess" earnings appears to apply in every case where "any carrier shall receive from operation in any year more than a fair return, to be determined by the Commission, upon the value of its property," even though the particular rates charged have been sustained, upon hearing, as just and reasonable.

It is difficult to understand upon what theory of proper regulation such rates are to be deemed to be unreasonable without any further inquiry as to the conditions of the service or as to matters directly relating to the rates themselves, but solely upon an inquiry with respect to the value of the carrier's property and the amount of the total net earnings derived by the carrier from its operations. The latter may be a legitimate inquiry for a court in determining whether a legislative body or its subordinate agency

has transcended its authority in fixing a body of rates so low as to be confiscatory. But it is a different thing thus to conclude that rates which are not confiscatory, and which as individual or joint rates have been expressly found in the case of the particular carrier to be just and reasonable for the services rendered were in fact not reasonable rates.

(2) Moreover, whether the rates which have produced the so-called "excess" earnings of the carrier have or have not been sustained in proceedings under Section 15 of the "Act to regulate commerce," as amended, with respect to the individual and joint rates of the particular carrier, the fact remains that the rates charged and collected have been fixed and maintained as just and reasonable rates, and that the Bill does not require as a necessary preliminary to the required payment of the "excess" that there should be a finding that the rates were in fact unreasonable rates. The only finding required is that a particular carrier has earned more than the amount which the Commission determines to be a "fair return" upon the value of its property held or used for the service.

The argument in support of the provision seems to assume that Congress, under the guise of regulating rates, either directly or through the Commission, can abandon the fixing of what are reasonable rates for the services rendered by the carrier, and without any determination that the particular rates or the tariff schedule of a carrier are unreasonable, take the earnings of a carrier simply upon a determination that

the carrier has received an "excess" over a "fair return" upon the value of its property.

This would appear to be not a regulation of rates, or of service, but of earnings. I do not understand that it is within the authority conferred upon Congress to regulate interstate commerce to determine how much a carrier not exercising a Federal franchise, or operating under a Federal contract, shall earn in interstate commerce, assuming that the carrier discharges all the public obligations incident to its service and charges reasonable rates. In my view the regulation of such a carrier must have direct relation to the services it renders and if the question is of the amount of money it should receive for its service, to the reasonableness of its charges.

(3) Again, if the assumption could be indulged that the finding that a carrier has received more than a "fair return," is to be regarded as tantamount to a finding that the rates which produce the "excess" earnings are unreasonable rates, and that such a finding without an inquiry with respect to the rates themselves, but only as to earnings, could be sustained, there would be a further difficulty.

I lay on one side the question of the propriety of treating rates as being reasonable as to one carrier and as being unreasonable as to another carrier with respect to substantially the same services under similar conditions.

Assuming that it is the intent of the provision that the rates producing the "excess" earnings in the case of a particular carrier are to be deemed to be un-

reasonable as to that carrier, there is manifestly a question beyond that of the right of that carrier to complain. As I have said, the provision applies to "excess" earnings received under rates, although these may have been sustained as just and reasonable after full hearing in proceedings instituted on the complaint of shippers or on the initiative of the Commission itself. The rates as originally fixed may have been sustained and shippers denied reparation. Or the rates as originally fixed may have been modified and the rights of shippers to reparation determined accordingly. Still, notwithstanding the rates are finally fixed and enforced as against shippers, the provision assumes the right to take the "excess" earnings obtained under such established rates on the theory that such rates are to be deemed unreasonable. Manifestly, in such case, the question of the validity of such a provision in the exercise of the regulating power is not exhausted by the mere consideration of what amounts to confiscation of the carrier's property.

Unreasonable rates constitute an unjust exaction from shippers or passengers. The rates maintained by Congress, or under its authority, in the exercise of its power of regulation of interstate commerce, are lawful because deemed to be reasonable, a presumption which the courts entertain, so long as the rates lie within the range of legislative discretion. But if we proceed on the assumption that the rates which are actually charged are extortionate, it would appear to be an abuse of the regulating power of Congress to enforce them. Congress, it may be said,

could not, under the guise of regulating interstate commerce, compel shippers or passengers to pay confessedly extortionate charges for the services rendered. On the hypothesis that the charges are unreasonable, the power to authorize them, no less than the power to collect them, falls. The exaction and maintenance of such charges would deprive shippers and passengers of their property without due process of law.

But it may be said that the rates which produce the "excess" earnings are to be regarded as unreasonable only with respect to the carrier, under the rule limiting its aggregate earnings, but that at the same time the rates maintained with respect to the persons paying the rates are to be regarded as reasonable as to such persons, and that the reasonableness of the rates with respect to shippers or passengers, although the rates are deemed to be unreasonable with respect to the carrier, may be sustained because they are based on average conditions and because of the use of the "excess" earnings for the benefit of shippers or passengers generally in aiding weak systems of transportation which are public utilities.

I regard this as a fallacy. I do not understand that rates charged by a carrier for the services it renders can properly be regarded as unreasonable with respect to the carrier and at the same time as reasonable with respect to those who pay the rates. The question of the reasonableness of the rates is essentially a question whether the charge made by the carrier and paid by the shipper or passenger for the service rendered is a charge which the shipper or passenger should pay

to the carrier and the carrier should receive for that service. If it is established that the rate is a reasonable one for a shipper or passenger to pay, it is the carrier that renders the service for which the rate is to be paid and it is proper that the carrier lawfully performing the service, and furnishing all the required facilities therefor, should receive and enjoy the proceeds of the rate thus charged. An attempt to divest the carrier of any portion of its earnings thus obtained, on the theory that the charges which it was reasonable for shippers and passengers to pay for its services it was unreasonable for the carrier to receive and retain would, in my judgment, be outside the scope of appropriate and valid regulation. The mere fact that it is proposed to devote the moneys or property of a carrier or of any other person to good uses cannot be regarded as justifying the deprivation of the carrier or such person of the right to enjoy and retain his own property, except as it may be taken for proper governmental purposes through valid taxation, or for public use on the payment of just compensation.

For the reasons stated, I am constrained to the conclusion that the provision in Section 6 of the pending Bill as to the payment of "excess" earnings, in its application to carriers not operating under a Federal franchise or contract permitting the imposition of such a condition, violates the Federal Constitution.

I remain,

Very respectfully yours,

(Signed) CHARLES E. HUGHES.